

REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA

**FINANCIAL AUDIT REPORT
CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
YEAR ENDED JUNE 30, 1981**

REPORT BY THE
OFFICE OF THE AUDITOR GENERAL
TO THE
JOINT LEGISLATIVE AUDIT COMMITTEE

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FINANCIAL AUDIT REPORT
CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
YEAR ENDED JUNE 30, 1981

NOVEMBER 1982



California Legislature

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November 17, 1982

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The Honorable President pro Tempore of the Senate
The Honorable Speaker of the Assembly
The Honorable Members of the Senate and the
Assembly of the Legislature of California

Members of the Legislature:

Your Joint Legislative Audit Committee respectfully submits the Auditor General's financial audit report of the California Student Aid Commission's State Guaranteed Student Loan Program, year ended June 30, 1981.

Respectfully submitted,

Walter M. Ingalls
WALTER M. INGALLS
Chairman, Joint Legislative
Audit Committee

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INTRODUCTION

In response to a request approved by the Joint Legislative Audit Committee, we have conducted a financial audit of the California Student Aid Commission's State Guaranteed Student Loan Program. The California Student Aid Commission (commission) requested this audit to meet its obligation to provide audited financial statements to lenders participating in the loan program. The Office of the Auditor General also conducted a performance audit of the State Guaranteed Student Loan Program as well as other programs of the commission. Our April 1982 report entitled, "A Review of the Student Aid Commission's Administration of Major Student Aid Programs" (Report No. P-015), presents the results of this performance audit. We conducted the present audit under the authority vested in the Auditor General by Section 10500 et seq. of the Government Code.

Chapter 1201, Statutes of 1977, established the State Guaranteed Student Loan Program and authorized the California Student Aid Commission to serve as a guarantee agency for student loans. This program carries out the provisions of the Federal Guaranteed Student Loan Program instituted within the Federal Higher Education Act of 1965 as amended (Education

Code, Section 69760). The commission is responsible for guaranteeing federally reinsured loans that are issued to eligible students.

The commission has contracted with United Student Aid Funds, Inc., a nonprofit corporation, for administrative support services. These services include processing and approving all student loan applications, managing guaranteed loans, processing claims from lenders, and preparing reports required by the United States Office of Education.

The State Guaranteed Student Loan Program is supported primarily by insurance premiums paid by student borrowers, federal funds, and investment earnings.

AUDITOR'S OPINION

We have examined the balance sheet of the California Student Aid Commission's State Guaranteed Student Loan Program as of June 30, 1981, and the related statement of revenues, expenditures, and changes in fund balance for the year then ended. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the California Student Aid Commission's State Guaranteed Student Loan Program at June 30, 1981, and the results of operations and changes in fund balance for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

OFFICE OF THE AUDITOR GENERAL



By: Karl W. Dolk, CPA
Assistant Auditor General

Date: May 24, 1982

Staff: Curt Davis, CPA, Audit Manager
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CALIFORNIA STUDENT AID COMMISSION
 STATE GUARANTEED STUDENT LOAN PROGRAM
BALANCE SHEET AT JUNE 30, 1981

ASSETS

Cash and investments (Note 2)	\$12,424,669
Accounts receivable (Note 3)	258,358
Due from other funds (Note 4)	1,180,993
Due from other governments (Note 5)	2,622,564
Equipment	<u>50,207</u>
 Total Assets	 <u>\$16,536,791</u>

LIABILITIES AND FUND EQUITY

Liabilities:

Due to other funds (Note 6)	<u>\$ 1,154,883</u>
 Total Liabilities	 <u>1,154,883</u>

Fund Equity:

Investment in fixed assets	<u>50,207</u>
 Fund Balance:	

Reserved for loan defaults (Note 8)	9,920,941
Designated for federal advance (Note 7)	2,150,153
Undesignated	<u>3,260,607</u>
 Total Fund Balance	 <u>15,331,701</u>

Total Fund Equity	<u>15,381,908</u>
 Total Liabilities and Fund Equity	 <u>\$16,536,791</u>

The notes to the financial statements are an integral part of this statement.

CALIFORNIA STUDENT AID COMMISSION
 STATE GUARANTEED STUDENT LOAN PROGRAM
 STATEMENT OF REVENUES, EXPENDITURES, AND
 CHANGES IN FUND BALANCE
FOR FISCAL YEAR ENDED JUNE 30, 1981

Revenues:

Insurance premiums (Note 10)	\$ 9,492,185
Intergovernmental revenue (Note 5)	2,888,449
Interest (Note 2)	909,313
Miscellaneous income	<u>153,364</u>
 Total Revenues	 <u>\$13,443,311</u>

Expenditures:

Personal services	\$ 508,016
Operating expenses and equipment	205,162
Contract fees (Note 12)	1,881,869
Interest	72,968
Miscellaneous expenditures	<u>101,615</u>
 Total Expenditures	 <u>2,769,630</u>
 Excess of Revenues Over Expenditures	 10,673,680
 Fund balance July 1, 1980	 <u>4,658,020</u>
 Fund balance June 30, 1981	 <u>\$15,331,701</u>

The notes to the financial statements are an integral part of this statement.

CALIFORNIA STUDENT AID COMMISSION
STATE GUARANTEED STUDENT LOAN PROGRAM
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1981

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying financial statements reflect the financial position and results of operations of the State Guaranteed Student Loan Program of the California Student Aid Commission (commission). The statements have been prepared in conformity with generally accepted accounting principles applicable to state and local governments as prescribed by the American Institute of Certified Public Accountants and by the National Council on Governmental Accounting. Below is a summary of the more significant accounting policies.

Fund Accounting

The State Guaranteed Student Loan Program is accounted for separately as a part of the State Guaranteed Loan Reserve Fund. The State Guaranteed Loan Reserve Fund was created to account for all monies received for guaranteeing loans to college students and to account for reimbursements to lending institutions for defaulted student loans.

This fund is accounted for as an Expendable Trust Fund. Expendable Trust Funds are used to account for assets held by the governmental unit as a trustee or as an agent for individuals, private organizations, other governmental units, and other funds.

Basis of Accounting

Expendable Trust Funds are accounted for on a modified accrual basis of accounting. Revenues are recognized in the accounting period in which they become measurable and available. Expenditures are recognized, if measurable, in the accounting period in which the liability is incurred.

Vacation and Sick Leave

Costs of vacation and sick leave are charged at the time these benefits are used rather than when they are earned.

2. CASH AND INVESTMENTS

This account represents cash in the state treasury. It also includes temporary cash reserves of program funds transferred to the Surplus Money Investment Fund for cash flow and pooled investment purposes. As of June 30, 1981, the balance of this account included cash in the state treasury of \$10,669 and a cash reserve for investment of \$12,414,000. Interest earned from investments of the Surplus Money Investment Fund are apportioned to the contributing funds on June 30 and December 31, based on the average daily cash balance of each fund. Interest due from the Surplus Money Investment Fund is accrued at June 30.

3. ACCOUNTS RECEIVABLE

This account represents insurance premiums collected by United Student Aid Funds, Inc., during June 1981. The commission received the premium payments from this corporation in July 1981.

4. DUE FROM OTHER FUNDS

This account includes \$563,494 due from the Surplus Money Investment Fund for interest earned. (See Note 2.)

The remaining balance of this account, \$617,499, is due from the General Fund for insurance premiums collected by the General Fund but not remitted to the State Guaranteed Loan Reserve Fund as of June 30, 1981.

5. DUE FROM OTHER GOVERNMENTS

This account represents the June 30, 1981 balance due from the United States Secretary of Education for the invoiced amounts for reimbursement of administrative costs. The amounts apply to administrative costs incurred between October 1, 1980 and June 30, 1981, and were paid in fiscal year 1981-1982. Under present procedures the California Student Aid Commission invoices the United States Secretary of Education for reimbursement of one percent of the balance of loans guaranteed, or actual administrative costs, whichever is less. Whether or not the Secretary pays the invoice is dependent upon the availability of federal funds.

6. DUE TO OTHER FUNDS

This account represents those operating costs incurred by the General Fund on behalf of the State Guaranteed Student Loan Reserve Fund during June 1981.

7. DESIGNATED FOR FEDERAL ADVANCE

Before 1967, the United States Secretary of Education advanced to the California Student Aid Commission \$1,479,865 for the Guaranteed Loan Program, which existed at the time; the Guaranteed Loan Program is referred to as the "old program." Additionally, the commission received another advance of \$1,079,211 for the revised loan program. The revised loan program, titled the State Guaranteed Student Loan Program, was enacted in 1977 and is referred to as the "new program." The total of the two advances is \$2,559,076. These advances were made under an agreement between the U.S. Secretary of Education and the California Student Aid Commission. In part, this agreement states as follows:

The Secretary may call upon the Agency for repayment of part or all of any sums advanced to the Agency hereunder, at such times and to the extent that he determines, in the light of the maturity and solvency of the Fund and after taking into account the Agency's requirements for its then outstanding obligations as well as its requirements for future loans and commitments based on its prior performance and established trends, that to do so will best carry out the purposes of the Act.

Although reported separately, both programs are accounted for in the State Guaranteed Loan Reserve Fund. As of June 30, 1981, the "old program" fund balance was \$408,923. Consequently, the remaining advance balance of \$2,150,153 could be payable from the State Guaranteed Student Loan Program fund balance.

8. RESERVED FOR LOAN DEFAULTS

The commission must maintain a reserve for the repurchase of defaulted loans. The commission is required to initially deposit at least 80 percent of the insurance premium revenue to this reserve. These funds can be used only for the purpose of purchasing defaulted loans. Total insurance premiums collected to date amount to \$12,401,176.

9. LENDERS' AGREEMENTS

The commission's agreements with lending institutions require that it maintain a Guarantee Reserve Fund. This fund must be represented by cash and marketable securities having a market value of not less than one percent of the total amount of unpaid principal and interest of all approved notes that are covered by federal reinsurance under the agreement between the commission and the U.S. Commissioner of Education. At June 30, 1981, the commission's cash and marketable securities exceeded the amounts required.

10. INSURANCE PREMIUMS

Student borrowers pay insurance premiums when their loans are disbursed by the lending institution. The premiums may be used to underwrite defaulted loans and to cover costs that the commission incurs in administering the loan program.

11. RETIREMENT COMMITMENTS

Regular employees of the commission are members of the Public Employee's Retirement System (PERS), which is a defined benefit, contributory retirement plan. The amount that the commission and its employees contribute to the PERS is actuarially determined under a program in which contributions plus retirement system earnings provide the necessary funds to pay retirement costs as accrued. The State Guaranteed Student Loan Program's share of retirement contributions for the year totaled \$56,001.

12. CONTRACT FEES

This figure represents amounts paid to United Student Aid Funds, Inc., for administrative support services. The fees are calculated as a percentage of the total amount of loans outstanding at the end of each month.

13. FEDERAL REINSURANCE AGREEMENT

The agreements between the California Student Aid Commission and the lenders participating in the loan program require that the commission purchase guaranteed loans that have been defaulted if the lender has exercised due diligence in making, servicing, and collecting the loan. Likewise, the agreement between the commission and the U.S. Secretary of Education requires the Secretary of Education to purchase a percentage of the defaulted loans purchased by the commission. Through federal fiscal year

1982-83, the U.S. Secretary of Education will purchase 100 percent of the defaulted loans. For federal fiscal year 1983-84 and after, the percentage of defaulted loans purchased by the U.S. Secretary of Education may decrease depending on the default rate from the State Guaranteed Student Loan Program.

OTHER COMMENTS

As an integral part of our examination, we reviewed the accounting procedures of the California Student Aid Commission (commission) and its related system of internal accounting control to the extent we considered necessary to properly form an opinion concerning the fairness with which the State Guaranteed Student Loan Program's financial statements present the program's financial position and the results of operations in accordance with generally accepted accounting principles consistently applied. As part of our review, we issued a management letter to the commission suggesting action that it should take to assure that it receives the funds it is entitled to. Our letter also recommended adjusting entries necessary to achieve compliance with generally accepted accounting principles. The commission is taking action to assure that it receives the funds it is entitled to and concurs with the adjusting entries.

cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Director of Finance
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps